

***United States Court of Appeals
for the Second Circuit***



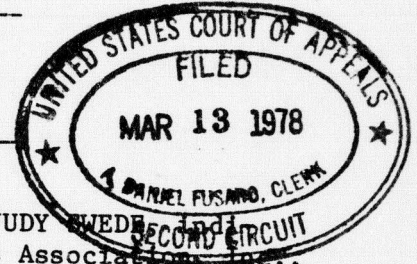
**APPELLANT'S
REPLY BRIEF**

77-6218

77-6218

To be argued by
Marc Kahn

UNITED STATES COURT OF APPEALS
For the Second Circuit



LYNN ARGO, ARNOLD ARGO, HELEN DENNIS, JAY GROSSMAN, JUDY SWEDER, individually and as Directors of Birchwood Towers Tenants Association, Inc., MAX WULFSON and DORA FRIEDMAN, individually and BIRCHWOOD TOWERS TENANTS ASSOCIATION, INC.,

Plaintiffs-Appellants

-against-

PATRICIA HARRIS, individually and as Secretary of Housing and Urban Development of the United States; MORRIS SOSNOW, KATE SOSNOW, LEONARD R. SCHWARTZ, JERROLD A. LIEBERMAN, BERNICE LIEBERMAN, and LORRAINE S. SANFORD, doing business as Birchwood Towers #1 Associates and doing business as Birchwood Towers #2 Associates; THE CONCILIATION AND APPEALS BOARD,

Defendants-Appellees,

-and-

THE HOUSING AND DEVELOPMENT ADMINISTRATION OF THE CITY OF NEW YORK,

Defendant-Cross Appellant.

On Appeal of a Preliminary Injunction, pursuant to 28 U.S.C. Section 1292 (a)(1), from the United States District Court for the Eastern District of New York.

APPELLANTS' REPLY BRIEF

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TABLE OF CONTENTS

	PAGE
PRELIMINARY STATEMENT.....	1
POINT I--The District Court Clearly Erred In the Preliminary Injunction by Ordering the Retroactive Application of the HUD Preemption Order of October 11, 1977.....	2
POINT II--The Owners' Reliance On the Consent Order of November 12, 1976 is Without Merit.....	4
POINT III--The Cases Relied Upon by the Owners as Authorities for the Preliminary Injunction Appealed from are Inapposite to the Case at Bar.....	6
POINT IV--The Cases Relied Upon by HUD are Similarly Inapposite to the Issues Before this Court.....	9
POINT V--The Owners' Conduct Throughout the Course of this Litigation Belies Its Claim of Irreparable Injury	10
CONCLUSION.....	12

Cases Cited

	PAGE
Adams Nursing Home of Williamstown, Inc. v. Mathews, 548 F.2d 1077 (1st Cir. 1977).....	9
Burr v. New Rochelle Municipal Housing Authority, 479 F.2d 1165 (2d Cir. 1973).....	3
Calder v. Bull, 3 U.S. (3 Dall.) 305, 306-307 (1798)...	8
Fisch v. General Motors Corporation, 169 F.2d 266 (6th Cir. 1948).....	8
Grace Towers Tenants Association v. Grace Housing De- velopment Fund Co., Inc., 538 F.2d 491 (2d Cir. 1976).....	8
Greene v. United States, 376 U.S. 149, 160 (1964).....	8
Keller v. Kate Maremount Foundation, 365 F.Supp. 798 (N.D. Cal. 1972).....	6, 7
Klein v. Department of Housing and Urban Development, F.Supp. (E.D.N.Y. 7/12/76) 76 C.374 T.C.P.....	7
Langevin v. Chenango Court, Inc., 447 F.2d 296 (2d Cir. 1971).....	6, 7
Marlboro Corp. v. Association of Independent Colleges, 556 F.2d 78 (1st Cir. 1977).....	9, 10
Mathews v. Eldridge, 424 U.S. 319 (1976).....	9
Ponce v. Housing Authority of the County of Tulare, 389 F.Supp. 635 (E.D. Cal. 1975).....	6, 7
Sobel Corrugated and Wooden Box Co., v. Fleming, 165 F.2d 568 (6th Cir. 1948).....	7

	PAGE
Usery v. Turner Elkhorn Mining Co., 428 U.S. 1 (1976)...	9

Rules Cited

24 C.F.R. 403 (1975).....	2,3,8
24 C.F.R. 401 (1975).....	8

Statutes Cited

Rent Stabilization Law of 1969, New York City Administrative Code, Sec. YY51-1.0.....	3
---	---

Other Authorities Cited

U.S. Constitution, Fifth Amendment.....	1,7
Code of the Rent Stabilization Association of N.Y.C., Inc., Sec. 40.....	2

PRELIMINARY STATEMENT

Appellants have been served with briefs by the Defendants-Appellees, Patricia Harris, the Secretary of the United States Department of Housing and Urban Development (HUD) and Morris Sosnow et al. (the owners). Each merits a brief reply.

The owners in their brief concede at page 14, that HUD could not preempt local rent controls and affect rent increases without providing due process to the tenants. Nevertheless, the owners stand the due process clause of the Fifth Amendment on its head by insisting that the District Court may properly coerce the taking of rent increases authorized by the invalid HUD order of September 1, 1976 (the first preemption order) (14a)* and collected prior to HUD's compliance with the rudimentary procedural due process protections set forth in the District Court's opinion of January 13, 1977 (the opinion) (66a). The Appellants respectfully submit that the Fifth Amendment's purpose of discouraging arbitrary government conduct is ill served by the owners' argument.

*Page references are to the Appendix unless otherwise noted.

POINT I

THE DISTRICT COURT CLEARLY ERRED IN THE PRELIMINARY INJUNCTION BY ORDERING THE RETROACTIVE APPLICATION OF THE HUD PREEMPTION ORDER OF OCTOBER 11, 1977

The owners' effort to enjoy the fruits of an administrative order held to be invalid by the District Court in its opinion of January 13, 1977 (at 80a) rests on the assertion that the District Court properly read the HUD order of October 11, 1977 to apply retroactively. The owners contend that since the second preemption order was issued in compliance with procedural due process, it should apply retroactively. This assertion is simply wrong. The preliminary injunction appealed from (125a) significantly changes the October 11th order by making it retroactive, a result nowhere articulated in the text of the order itself and nowhere contemplated or authorized by the pre-emption regulation, 24 C.F.R. Sec. 403.1 et seq. (6a).*

*Note, by comparison, §40 of the Amended Code of the Rent Stabilization Association of N.Y.C., Inc. [enacted pursuant to the Rent Stabilization Law of 1969], which explicitly provides for the retroactive application of rent increase orders. The pertinent portion of section 40 reads as follows:

An application for the adjustment of a stabilization rent may be filed on any grounds specified herein. In the event no order is issued within thirty (30) days from the date of filing an application before the CAB, the order adjusting the stabilization rent shall be effective as of such thirtieth date.

The text of the rule evidences only a prospective application of a preemption determination. The Rule provides, at 403.6(f), for the collection of HUD approved rents after the expiration of thirty (30) days' notice to the tenants (6a).

The District Court's reading of the second preemption determination to "reaffirm retroactively" (127a) the earlier invalid determination is not only contrary to the text of the Rule, but is also contrary to the District Court's opinion, citing Burr v. New Rochelle Municipal Housing Authority, 479 F.2d 1165, 1170 (2d Cir. 1973), that HUD's preemption of the Rent Stabilization Law, New York City Administrative Code, Sec. YY51-1.0 could not validly take place until procedural due process requirements were met, including the exposition of a written statement justifying preemption (81a, 82a). Since this latter requirement was not satisfied until October 11, 1977, no preemption of the local rent control law or concomitant rent increase "taking" could properly be imposed prior to that date.

The order appealed from specifically recites the same requirements (126a). HUD too has finally accepted its constitutional duty to accord procedural due process prior to preemption, and has circulated a proposed amendment to Rule 403.1, a copy of which is appended hereto as Exhibit A. In addition to setting forth due process requirements, the proposed Rule unmistakably provides for prospective increases

only. Owners are required to inform tenants that, "When HUD advises us in writing of its decision on our request, you will be notified at least 30 days before any change in the rental structure is put into effect...." See, Ex. A at §403.7. After a preemption certificate has issued, the owner can effect collection of the HUD rents after the expiration of 30 days' notice to the tenants. Ex. A at §403.11(c) and (d). It would be anomalous indeed to sustain the District Court's incorrect reading of the second preemption order after HUD has acceded to Appellants' position. For these reasons, it is respectfully submitted that the District Court erroneously applied the second preemption order retroactively.

POINT II

THE OWNERS' RELIANCE ON THE CONSENT ORDER OF NOVEMBER 12, 1976 IS WITHOUT MERIT.

It should be noted that the consent order of November 12, 1976 supports the Appellants' position and totally justifies the Appellants' request that the order appealed from be set aside, and the funds collected prior to October 11, 1977 be disbursed to the Appellants.

Paragraph 4a of the order (64a) explicitly states that:

in the event it is finally determined after any appeals which may be taken by any party that the preemption of local rent control by HUD as to Birchwood Towers was not valid and/or that the landlord is not entitled to any increase in rental other than that provided for by CAB, the money paid in escrow pursuant to paragraphs 3 above, by each tenant-member shall be returned to such tenant-member without interest [emphasis added].

The Court's opinion held precisely that the preemption pursuant to the first HUD order of September 1, 1977 was not valid because it was implemented without due process for the tenants (80a). The owners' reliance on the consent order is clearly misplaced. Under the agreement, the escrowed funds must be disbursed to the Appellants.*

The consent order was subject to further order of the court. Subsequent orders of the District Court have, in fact, modified that order. There is no provision in the November 1976 order consenting to payment of rent increases pursuant to an invalid HUD order, or consenting to retroactive payments under any future order HUD might issue. The agreement was only intended to maintain the status quo pending a final determination by the Court, which was made two

*Although there may be issues in this case which have not been "finally determined," the issue of whether this initial pre-emption of local rent controls by HUD was not valid is not one of them. That issue was determined in favor of the Appellants in the Court's opinion and order of January 13, 1977, and the Appellees' time to appeal from that order has long since expired.

(2) months later in the opinion of January 13, 1977, in which Appellants prevailed on their procedural due process claim.

POINT III

THE CASES RELIED UPON BY THE OWNERS AS AUTHORITIES FOR THE PRELIMINARY INJUNCTION APPEALED FROM ARE INAPPOSITE TO THE CASE AT BAR

The owners strenuously insist that the cases of Keller v. Kate Maremount Foundation, 365 F.Supp. 798 (N.D. Cal. 1972) and Ponce v. Housing Authority of the County of Tulare, 389 F.Supp. 635 (E.D. Cal. 1975) justify and support the disposition of the escrow funds under the District Court's preliminary injunction. This might be true if the cases cited involved the preemption or deprivation of property interests or "legitimate expectations" arising under a local rent control law. They did not. Instead, each of these cases merely involved a rent increase for low income subsidized housing projects imposed by HUD in the absence of any local rent control limitation, much like the case of Langevin v. Chenango Court, Inc., 447 F.2d 296 (2d Circ. 1971). Under the Langevin decision, tenants in such circumstances are not entitled to due process protections and would have no right to dispute the taking of these rent increases without due process. In Langevin,

Judge Friendly limited the applicability of the decision to situations in which "no Federal, State or local law required more." 447 F.2d at 301.

At least one District Court in this circuit has explicitly applied the distinction between Langevin and the case at bar in which a protected property interest, i.e. the legitimate expectation arising from the Rent Stabilization Law, is to be "taken." Klein v. Department of Housing and Urban Development, ____ F.Supp. ____ (E.D.N.Y. 7/12/76) (76 C. 374 T.C.P.). Unlike the Keller and Ponce cases, it is the intrusion upon local rent controls, and the arbitrary preemption of those controls which offends the Fifth Amendment and makes the remedy of Ponce and Keller improper here.

The case of Sobel Corrugated & Wooden Box Co. v. Fleming, 165 F.2d 568 (6th Cir. 1948) is not at all germane to the issues in dispute on this appeal. The plaintiff in that case was clearly under a duty to comply with a price reporting regulation affecting all manufactures in a given class. Plaintiff failed to comply with that regulation and was brought before the price administrator for a hearing to determine the plaintiff's past conduct. In our case, the complaining parties are not subject to a regulation which applies across the board to every mortgage insured by HUD. By contrast, our case involves an adjudicatory type of proceeding in which the rights and liabilities of certain

individuals were arbitrarily assigned without notice or opportunity to participate.

The owners' citation of Fisch v. General Motors Corporation, 169 F.2d 266 (6th Cir. 1948) in support of the proposition that retroactive application of civil laws are not constitutionally prohibited, does little to illuminate the owners' conclusion that there is no defect in the retroactive application of an administrative order. The considerations underlying the retroactive application of statutes and rules are not identical to those governing the application of an administrative order. In any event, there are few principles of construction more venerable than the rule that civil laws are prospective in effect and will not be given a retrospective operation unless that is the unequivocal and inflexible import of its terms, and the manifest intention of the legislature. Greene v. United States, 376 U.S. 149, 160 (1964); Calder v. Bull, 3 U.S. (3 Dall.) 305, 306-307 (1798).

As noted above, the text of Rule 403.1 makes no provision for retroactivity (6a). In Grace Towers Tenants Association v. Grace Housing Development Fund Co., Inc., 538 F.2d 491 (2d Cir. 1976), this court declined to apply 24 C.F.R. Sec. 401 retroactively. The Court should again decline to condone the District Court's unprincipled retroactive application of the second preemption order.

POINT IV

THE CASES RELIED UPON BY HUD ARE SIMILARLY IN-
APPOSITE TO THE ISSUES BEFORE THIS COURT

The brief submitted by HUD discusses several cases which consider the retrospective imposition of liability under a statute or regulation. See, e.g., Usery v. Turner Elkhorn Mining Co., 428 U.S. 1 (1976) and Adams Nursing Home of Williamstown, Inc. v. Mathews, 548 F.2d 1077 (1st Cir. 1977). Again, the appeal before this Court does not turn upon the retroactive application of any statute or regulation.

In Usery and Adams, the statute and regulation respectively at issue were found to be valid, unlike the first preemption order in this case.

HUD cites the case of Mathews v. Eldridge, 424 U.S. 319 (1976) but concedes that Mathews held that a prior hearing was constitutionally mandated under the facts of that case. Similarly, in the case of Marlboro Corp. v. Association of Independent Colleges, 556 F.2d 78 (1st Cir. 1977), the plaintiff did in fact receive the requisite procedural due process prior to the adjudication depriving it of its property interests. See, 556 F.2d at 80, 82. There was no retroactive application of the contested administrative order in that case, and the order itself was found to be

why the owner has assented to, and acquiesced in conduct which could only delay or prevent it from obtaining the relief it initially sought. Why, for example, did the owner draft and agree to the consent order of November 12, 1976 which provided for the escrow of the disputed HUD rent increases? Why did the owner subsequently acquiesce in the District Court's opinion which effectively deprived it of the desperately needed escrow funds for an indefinite period of time? Why, if the owners "faced and still faces [sic] the immediate threat of default and foreclosure throughout these proceedings" (owners' brief at 17) did the owners draft and submit a preliminary injunction for signature which not only continued the escrow arrangement until final determination of this action and all appeals, but also provided for the escrow of additional tenant rentals until the final determination of this action (127a)? Why did the owners, after seventeen months of continuing litigation with no end in sight, fail to file a cross-appeal from the preliminary injunction or ask this Court for the relief it so desperately needs?

It is apparent that the irreparable injury perceived by the District Court was largely self-created and exacerbated by the owners' own conduct. For these reasons, the Appellants respectfully submit that the District Court

erred by finding irreparable injury on the part of the owner.

CONCLUSION

Appellants respectfully submit that the District Court's arbitrary and erroneous application of the second preemption order retroactively should be redressed, and request an order dissolving the preliminary injunction and disbursing to Appellants the funds collected in escrow prior to October 11, 1977.

Respectfully submitted,

Rosenstein & Kahn
Attorneys for Plaintiff--Appellants

Dated: New York, N.Y.

March 9, 1978

Marc Kahn
Barney Rosenstein, of counsel

Title 24 - DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Chapter IV - Office of Assistant Secretary for
Housing-Federal Housing Commissioner

/Docket No.

7

PART 403 - LOCAL RENT CONTROL

AGENCY: Office of Assistant Secretary for Housing-Federal Housing Commissioner, Department of Housing and Urban Development.

ACTION: Proposed Rule for Public Comments

SUMMARY: The Department of Housing and Urban Development is considering amendments to Part 403 of Title 24 of the Code of Federal Regulations in order to provide for tenant comments in the Department's preemption determination on unsubsidized projects. Additionally, clarification is provided as to procedures for determining the rents necessary to maintain and operate adequately the project.

FOR FURTHER INFORMATION CONTACT:

James J. Tahash, Director, Insured Project
Mortgage Division, Office of Loan Management,
Office of Insured and Direct Loan Programs,
Department of Housing and Urban Development
Washington, D. C. 20410 (202) 755-5757

SUPPLEMENTARY INFORMATION: The Department of Housing and Urban Development hereby propose to amend the Final Rule published on October 22, 1975 (40 F.R. 49318) on local rent control. The proposed rule sets forth new procedures for mortgagors of unsubsidized projects to follow when requesting HUD's preemption of local rent control regulation which provides for tenant comment in the preemption determination. These procedures include: notification to the tenants by the mortgagor of its intent to request preemption approval by HUD; (2) an

Ex. A

opportunity for tenants to examine materials supporting the mortgagor's proposed preemption request and to make written comments thereon to the mortgagor and to HUD; and (3) after HUD has considered all submitted material and made a determination, notification to the tenants by the mortgagor of the reasons for approval or disapproval. Additionally, the interim rule provides that preemption requests will be processed in accordance with special preemption instructions which will determine the rent necessary to maintain and operate adequately the project.

Written comments and suggestions will be received until _____ . HUD will make such modifications as it deems appropriate in the final regulations. Comments should be submitted to the Rules Docket Clerk, Office of General Counsel, Room 5218, Department of Housing and Urban Development, 451 Seventh Street, S.W., Washington, D. C. 20410. A copy of each communication will be available for public inspection during regular business hours at the above address.

The Department has determined that an Environmental Impact Statement is not required with respect to this rule. The Finding of Inapplicability in accordance with HUD's environmental procedures handbook (HUD Handbook 1390.1) is available for inspection at the Office of the Rules Docket Clerk, at the above address.

Accordingly, it is proposed that Part 403, of Chapter IV of 24 CFR be amended as follows:

Subpart B - Unsubsidized Insured Projects

1. Section 403.4 Applicability

* * *

2. Sections 403.5 through 403.11 have been revised as follows:

§ 403.5 Rental Charges.

The Department will generally not interfere in the regulation of rents by a rent control board or agency constituted under state or local laws (hereinafter referred to as board) for unsubsidized projects with mortgages insured or held by HUD. However, HUD will preempt the regulation of rents, as well as the term of prospective leases, for such a project when the Department determines that the delay or decision of a board, jeopardizes the Department's economic interest in the project.

§ 403.6 Initiation.

When a mortgagor determines that the permitted increase in rents as prescribed by a local rent control board will not provide the minimum rents necessary to maintain and operate adequately the project, the mortgagor shall

- (a) file its application for whatever relief or redetermination is permitted under the state or local law;

- (b) in accordance with § 403.7 of this subpart, notify the appropriate HUD office and the local board of its intention to file a request for preemption of local rent control regulations pursuant to the provisions of the regulations in this subpart.

§ 403.7 Notice to Tenants.

At least 30 days before filing a formal request to HUD for preemption of local rent control regulation, the mortgagor shall notify the tenants of its intention to so file. Copies of such notice shall be:

- (a) delivered directly or by mail to each tenant; or
- (b) posted in at least 3 conspicuous places within each structure or building in which the affected dwelling units are located.

The notice shall contain the addresses where the material in support of the preemption request are to be made available to tenants as well as the required information in the following format or equivalent thereto:

Notice To Tenants Of Intention To File
A Request To HUD For Preemption Of Local
Rent Control Regulation

Date of Notice

Take notice that on (date) we requested the
(_____ Name) board to review our application for
redetermination of permitted rents.

Take further notice that on (date), if the
(Name) board denies or fails to act
on our request, we plan to file a request for
preemption of local rent control regulation
for (name of apartment complex) with the United
States Department of Housing and Urban Develop-
ment (HUD). The requested preemption action
is needed for the following reasons:

- (1) HUD approved Gross Potential Income
Year Approved: _____ \$ _____
- (2) Current Total Residential Rents
Allowed by Local Rent Control
Board. _____ \$ _____
- (3) Projected Total Annual Residential
Rents Allowable Under Local Board
Regulations 6 Months After Date of
This Notice _____ \$ _____
- (4) Income Required to Operate Project
as Supported by Profit and Loss
Statement Being Submitted to HUD _____ \$ _____

Copies of the materials that we intend to submit to
HUD in support of our request will be available during
normal business hours at (address) for a period of 30
days from the date of this notice for inspection and
copying by tenants of (name of apartment complex) and,
if the tenants wish, legal or other representatives
duly authorized in writing to act for one or more of
the tenants.

During a period of 30 days from the date of this
notice, tenants of (name of apartment complex) may
submit written comments on the proposed preemption

request to us at (address). Tenant representatives may assist tenants in preparing those comments. The inspection and comment period will be extended as necessary to assure a 30-day comment period for a complete submission and to allow at least 5 days to comment on any supplemental material submitted in support of the application that are not available to the tenants during the first 25 days of the 30-day period. These comments will be transmitted to HUD, along with our evaluation of them and our preemption request. You may also send a copy of your comments directly to HUD at the following address: United States Department of Housing and Urban Development (address of local HUD field office with jurisdiction over preemption of rents for the project). Attention: Director, Housing

RE: Project No. (Name of Apartment Complex).

HUD will approve or disapprove the preemption request in whole or in part upon reviewing the materials and comments. When HUD advises us in writing of its decision on our request, you will be notified at least 30 days before any change in the rental structure is put into effect, in accordance with the terms of existing leases.

(Name of mortgagor or managing agent)

The mortgagor shall comply with all representations made in the Notice.

S 403.8 Materials to be Submitted to HUD.

- (a) After posting or distribution of the notice, the mortgagor shall immediately send HUD notification of its intention to file a preemption request, to include:
- (1) The written notice to the tenants, which will state the date of its posting and/or distribution;
 - (2) An annual Statement of Profit and Loss, on a form prescribed by the Commissioner, audited by an independent public accountant and covering the most recently ended accounting year, and an unaudited accrual Profit and Loss Statement on a form prescribed by the Commissioner for the intervening period since the date of the last annual statement if more than four months have elapsed since that date;
 - (3) A certified statement which provides a separate breakdown for the percentage of vacancies for the present and previous year.
 - (4) A certified statement which provides a separate breakdown of the actual rent loss due to non-payment of rent for the past two years.
 - (5) A certified statement which provides a separate breakdown of rent loss due to tenant turnover for the past two years.

- (6) A certified statement covering known approved rate or cost increases not yet experienced by the project which can be documented:
 - (a) Tax rates or appraisals
 - (b) Utility rates
 - (c) Contracts for employees or services
 - (d) Insurance
 - (7) A certified statement covering known decreases of rates or costs not yet experienced by the project which have been approved and can be documented. If none, so certify.
 - (a) Tax rates or appraisals
 - (b) Utility rates
 - (c) Contract for employees or services
 - (d) Insurance
 - (8) A copy of the full application to the board with supporting documentation.
- (b) The local HUD office shall promptly, upon receipt, review the mortgagor's submission to ascertain that it is complete as required by paragraph (a) of this Section. Should the submission be found incomplete, the local HUD office shall notify the mortgagor within 48-hours of said review of its determination that further material is necessary to constitute a complete submission as defined in paragraph (a) of this Section.

- (c) When the submission is complete, the HUD office shall hold the mortgagor's submission as specified in (a) of this Section in abeyance during the 30 day comment period.

§ 403.9 Request for Preemption.

- (a) Upon expiration of the period for tenant comments required in the notice format and after review of the comments submitted to him, the mortgagor shall submit, in addition to the material enumerated in § 403.8 and any revisions thereto, his preemption request together with the following:
- (1) A certification by the mortgagor following the requirements specified in § 403.9(b);
 - (2) Copies of all written comments submitted by the tenants to the mortgagor;
 - (3) The mortgagor's evaluation of the tenants' comments with respect to the request; and
 - (4) The board's decision or a statement certifying that a decision from the board has not been received.
- (b) The certification of the mortgagor as required by § 403.9(a)(1) shall attest:
- (1) That the Notice required by § 403.7 was given pursuant to the provisions of that Section;
 - (2) That the mortgagor has taken reasonable steps to assure that the substance of the Notice has been conveyed to each resident household, and

in cases where the Notice was posted, that the mortgagor exercised its best efforts to assure that the Notices were maintained intact and in legible form for the specified thirty (30) days;

- (3) That the copies of the materials submitted in support of the preemption request were located in a place reasonably convenient to tenants in the project during normal business hours and that requests by tenants to inspect such materials, as provided for in the Notice, were honored;

- (4) That copies of all comments received from the tenants were considered and are being transmitted to HUD together with the certification; and
 - (5) That "under the penalties and provisions of Title 18, United States Code, section 1001, the statements contained in this application and its attachments have been examined by me and, to the best of my knowledge and belief, are true, correct, and complete."
- (c) Should the mortgagor receive a delayed decision from the board after filing its preemption request, HUD shall be immediately informed and furnished with a copy.

§ 403.10 Notification of Action on Preemption Request.

After HUD has considered the preemption request which meets the requirements of § 403.9 and has made its determination to approve or disapprove the request, it will furnish the mortgagor with a written statement of the reasons for approval or disapproval. The mortgagor shall make known to tenants, by posting or delivery in the manner outlined in § 403.7 the reasons for approval or disapproval.

§ 403.11 HUD Procedures.

- (a) The mortgagor's preemption request will be processed in accordance with the preemption instructions, especially developed to determine the minimum rent level required to maintain and adequately operate the project.
- (b) The local HUD office will review the information submitted by the mortgagor, together with the decision of the board, if any, and shall make a report if it deems the delay or decision of the board jeopardizes the Department's economic interest in the project and the board will not modify its position to the satisfaction of the local HUD office. The report shall be sent to the Office of Loan Management, Headquarters, (hereinafter referred to as Office of Loan Management) and shall include appropriate recommendations concerning the action that should be taken by HUD.
- (c) The Office of Loan Management will review the report and will consider whether to preempt the board's regulation. Upon its findings that the protection of the Department's economic interest requires:
 - (1) higher rent levels than those approved by the board, or
 - (2) higher rent levels notwithstanding the delay of the board in reaching a decision, it shall issue

a formal certification to the local board that its authority has been preempted as to such rents in order to protect the Department's economic interest in the project. Copies of the certification shall be transmitted to the mortgagor, the local HUD office, and the board.

- (d) The mortgagor may effect collection of the HUD-approved jeopardy rent levels after the expiration of 30 days notice to the tenants, subject to the terms and rights a tenant may have under the existing lease.
- (e) In those instances where it will take more than 60 days (2 months) for the project to reach the new rent levels, HUD's preemption of prospective lease terms shall be effective on a prospective basis for those new or renewed leases which by regulation of a local rent control board would exceed a one-year term. To this effect, leases which expire during the preemption period shall not be renewed for longer than a one-year period.
- (f) Once the project reaches the rental level approved under these procedures, the project will be returned to the control of the local rent control board covering both the rents and the term of prospective leases.

It is hereby certified that the economic and inflationary impacts of this interim rule have been carefully evaluated in accordance with Executive Order No. 11821.

Lawrence B. Simons
Assistant Secretary for Housing-
Federal Housing Commissioner